FUTUREGROWTH
/ ASSET MANAGEMENT

Monthly Review

April 2016

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Market review

Economic and market review

Bond market extends recent gains	Bond yields declined for a second consecutive month. During April, the yield of the benchmark R186 (maturity 2026) closed 14 basis points lower at 8.96%, the lowest monthly closing level since November 2015. The temporary improvement in sentiment was the result of both foreign and local developments.
Sentiment boosted by improved risk appetite	Globally, the improvement in risk appetite supported commodities and emerging market currencies, thus benefiting the rand and local bonds. This is best illustrated by the sizeable net new investment in local bonds by foreign investors over this period. The combination of a perceived improvement in China's growth outlook, renewed interest in commodities in general, an undervalued rand against most other currencies and the wide interest rate differential between South Africa and developed economies lured these buyers into the local market, despite the dark cloud of an imminent foreign currency ratings downgrade.
Local data releases mostly interest rate friendly	Locally, the bond market received support from lower than expected headline CPI and PPI data releases even though this was mostly as a result of technical factors. A small external trade surplus and the extension of the contract of the director general of National Treasury, by another five years, also boosted investor sentiment. The March main budget data confirmed that the Ministry of Finance achieved a slightly lower deficit for 2015/16 than anticipated earlier this year. However, the challenge remains to reduce the budget deficit for the forthcoming fiscal years to the various challenging targets tabled in February's Budget, especially considering the downside risk to already weak economic growth.
Inflation-linked bonds best performing interest bearing asset	Meanwhile, inflation-linked bonds turned out to be the best performing interest-bearing asset over the month, on the back of a combination of falling real yields (reflecting the demand for inflation protection) and the positive impact of rising inflation on valuation. While Headline CPI accelerated at a slower pace over the last month or so, details point to more widespread price increases as cost pass through from broad based and sustained rand depreciation and the impact of the severe drought start filtering through. The JSE ASSA Inflation-linked Government Bond Index returned a strong 3.2% over the month, followed by the JSE ASSA All Bond Index or nominal bonds (1.9%) and cash in third place (0.5%).

Summary

Key macroeconomic themes

Economic growth	A mild cyclical and uneven global economic recovery remains our base case, with a stronger US economy leading the way. In contrast, euro zone growth remains challenged, and prospects for Japan look particularly poor. We believe that the global recovery would be structurally lower than in previous cycles, mainly due to low productivity growth, high leverage levels (albeit much improved from pre-crisis levels) and demographic factors (older populations tend to save more and spend less). Most emerging market economies are caught between a mixed outlook for the developed world, concern about the implications of weaker Chinese growth on commodity demand and the impact of the Federal Reserve's well telegraphed intent to normalise monetary policy. Commodity producers with large external imbalances, such as SA, remain particularly vulnerable.

Summary

Key macroeconomic themes

Economic growth	Locally, the biggest impediment to higher local growth remains structural, while the severity of the drought adds to the list of growth detractors. Encouragingly, overdue engagement between government and business raises the prospects of unbundling domestic growth potential – but prompt and practical follow through is still necessary to be impactful.
Inflation	Although recent data releases have quelled earlier excessive global deflation fears, expectations of rapid reflation are also misplaced. Global inflation trends are likely to remain subdued in our view. Locally, the combination of sustained and broad-based rand weakness and fast-rising food prices have pushed our 2016 and 2017 annual average inflation forecasts to 6.6% and 5.8% respectively. We shall be keeping one eye on the core measure of inflation for a more reliable indication of underlying inflationary pressure, which is still below 6%. Broader evidence of rand weakness pass through is starting to show, and this remains one of our main concerns.
Balance of payments	The combination of rand weakness and a marginally improved terms of trade position (partly due to lower crude oil prices), lends limited relief to the fragile balance of payment situation. As a result, we expect a narrowing in the current account deficit from an annual average of 5.2% in 2015 to 3.7% in both 2016 and 2017. Although this improvement is welcomed, we note with a fair degree of concern that SA is still saddled with a relatively weak external trade position which in turn will remain a drag on the currency. It remains a significant challenge to fund the shortfall considering the unsupportive global backdrop, low domestic real rates and the relative unattractiveness of SA as a longer-term investment destination.
Monetary policy	Having finally started the long awaited and well telegraphed monetary policy normalisation process, we agree with the Federal Reserve's intent to follow a slow and gradual process. The current trend of global monetary policy divergence is expected to continue over the next year or so. With more policy tightening in the US (and eventually in the UK) on the cards, the European Central Bank and Bank of Japan will retain their quantitative easing programmes. At the same time some of the smaller advanced and commodity driven economies may be forced to ease policy, mainly due to low growth and a modest inflation backdrop. On the positive side, monetary policy divergence will act to soften the impact of higher US rates on global growth. In the case of SA, we feel comfortable with the prospects of a very gradual tightening process, especially considering that the repo rate has already been increased by a cumulative 2% in this cycle. A cautious approach is supported by the weak economic growth backdrop, low levels of credit extension growth and limited evidence of demand-led inflation. Unfortunately, the monetary authorities cannot ignore rising cost pressures, especially those originating from food prices, energy prices and persistent currency weakness. Moreover, monetary policy, even if credible, cannot be considered in isolation. It goes hand in hand with fiscal prudence and a more balanced external account. Considering the size of the balance of payments deficit, the real repo rate remains too low. We expect this rate to be increased by another 50 basis points within the next twelve months.

Key macroeconomic themes continued

Fiscal policy

The minister of Finance delivered a realistic and balanced Budget in February, placing due emphasis on realism in light of a soft domestic growth outlook and questionable fiscal policy credibility. We now look for evidence of the planned consolidation path, cognisant of the elevated execution risk in the outer years of the Medium Term Expenditure Framework. The financial state of some state-owned enterprises, and the implications for a finely balanced fiscal position, remain a significant concern.

Investment view and strategy

The global growth recovery remains fragile and patchy, setting the scene for a more modest future global inflation profile as well as significant monetary policy divergence. It also implies a steady and shallow tightening cycle for the few economies (especially the US) that are in a position to normalise monetary policy. This should cap global bond yields especially as inflation pressures in developed markets remain subdued. On the negative side, the continued uncertainty about the Chinese growth outlook remains a risk, especially for emerging market commodity producers with a weak external position like South Africa.

Locally, investors face a worsening inflation outlook on the back of rising food prices, the risk posed by sustained rand weakness and the likely increase in inflation expectations. Although the Minister of Finance is clearly determined to rectify the damage to fiscal policy credibility and, by implication, a sovereign credit downgrade to non-investment status, the jury is still out on actual delivery. Besides South African idiosyncratic factors, we also expect global risk appetite to remain volatile. As a result, we will approach the market with caution and retain our holding of low duration inflation-linked bonds. Moreover, the South African Reserve Bank will need to raise the repo rate again, a move already anticipated by both the money and bond markets. We have assumed a non-investment sovereign rating by Standard & Poor's (S&P) in our valuation models.

At face value, this backdrop favours an overweight position in cash, underweight position in nominal bonds and the further accumulation of inflation-linked bonds. However, in acknowledgement of the fact that markets move fast in pricing risk (even the widely anticipated sub-investment downgrade by S&P), we would retain a small overweight exposure to long-dated nominal bonds in funds benchmarked against the All Bond Index (ALBI).

Our broad interest rate investment strategy for a core bond fund benchmarked against the ALBI is as follows:

- Modified duration - Underweight
- Cash - Overweight
- Nominal bonds (1-12 years) - Underweight
- Nominal bonds (15+ years) - Overweight
- Inflation-linked bonds - Overweight

Key economic indicators and forecasts
(annual averages)

	2012	2013	2014	2015	2016	2017
Global GDP						
USA	2.2%	1.9%	2.4%	2.4%	1.8%	2.0%
Euro area	0.1%	-0.4%	0.9%	1.5%	1.7%	1.8%
Japan	2.1%	1.6%	-0.1%	0.5%	0.5%	0.6%
China	7.8%	7.7%	7.4%	6.9%	6.6%	6.5%
SA GDP	2.2%	2.2%	1.5%	1.3%	0.8%	1.5%
SA Headline CPI	5.6%	5.8%	6.1%	4.6%	6.6%	5.8%
SA Current Account (% of GDP)	-5.2%	-5.8%	-5.4%	-3.9%	-3.7%	-3.7%

Source: Old Mutual Investment Group

Produced by

Wikus Furstenberg
Portfolio Manager &
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Product information and performance

Product	Benchmark	Description	Portfolio manager	Inception date	Investment returns	1 Year	3 Years*	5 Years*	7 Years*	10 Years*	Since inception*
MONEY MARKET											
Call Money Market	Average Call rate of four largest SA banks	Aims to provide maximum return on overnight cash investments.	Nazley Bardien	January 2000	Product Benchmark Outperformance	6.27% 5.83% 0.44%	5.66% 5.22% 0.44%	5.49% 5.01% 0.48%	5.80% 5.30% 0.50%		7.06% 6.57% 0.49%
Core Money Market	STeFI 3-month Index	Targets high cash returns through a carefully balanced and actively managed mix of short-term interest-bearing investments. The weighted average duration for the Composite may not exceed 120 days.	Michael van Rensburg	July 2004	Product Benchmark Outperformance	7.26% 6.31% 0.95%	6.52% 5.77% 0.75%	6.25% 5.59% 0.66%	6.62% 5.92% 0.70%	7.83% 7.11% 0.72%	7.81% 7.12% 0.69%
180 day Enhanced Money Market	STeFI Composite Index	Targets high cash returns through a carefully balanced and actively managed mix of short- and medium-term interest-bearing investments with maturities ranging from 180 days to 2 years.	Michael van Rensburg	July 2004	Product Benchmark Outperformance	7.54% 6.68% 0.86%	6.68% 6.05% 0.63%	6.45% 5.81% 0.64%	6.83% 6.07% 0.76%	8.00% 7.22% 0.78%	8.02% 7.21% 0.81%
STEFI PLUS											
Yield Enhanced A STeFI+ Short Term	STeFI Composite Index	Targets high cash returns through active interest rate risk management and yield enhancement. The Composite's weighted average rated credit quality must be a minimum of A-. Weighted average term to maturity less than 365 days.	Daphne Botha	October 2002	Product Benchmark Outperformance	7.84% 6.68% 1.16%	7.43% 6.05% 1.38%	7.48% 5.84% 1.64%	7.72% 6.21% 1.51%	8.69% 7.31% 1.38%	8.97% 7.80% 1.17%
Yield Enhanced A STeFI+	STeFI Composite Index	Targets high cash returns through active interest rate risk management and yield enhancement. The Composite's weighted average rated credit quality must be a minimum of A based on official ratings. Weighted average term to maturity less than five years.	Daphne Botha	January 2010	Product Benchmark Outperformance	8.93% 6.68% 2.25%	8.37% 6.05% 2.32%	8.07% 5.84% 2.23%			8.38% 6.01% 2.37%
Yield Enhanced BBB STeFI+	STeFI Composite Index	Targets high cash returns through active interest rate risk management and yield enhancement. The Composite's weighted average rated credit quality must be a minimum of BBB.	Daphne Botha	February 2010	Product Benchmark Outperformance	11.73% 6.68% 5.05%	10.62% 6.05% 4.57%	9.95% 5.84% 4.11%			9.98% 5.98% 4.00%

Product	Benchmark	Description	Portfolio manager	Inception date	Investment returns	1 Year	3 Years*	5 Years*	7 Years*	10 Years*	Since inception*
STEFI PLUS CONT.											
Yield Enhanced BB STeFI+	STeFI Composite Index	Targets high cash returns through active interest rate risk management and yield enhancement. The Composite's weighted average rated credit quality must be a minimum of BB.	Daphne Botha	January 2012	Product Benchmark Outperformance	13.45% 6.68% 6.77%	13.76% 6.05% 7.71%				12.28% 5.86% 6.42%
Yield Enhanced Geared BB STeFI+	STeFI Composite Index	Targets high cash returns through active interest rate risk management and yield enhancement, as well as equity risk. The Composite's weighted average rated credit quality must be a minimum of BB-.	Daphne Botha	January 2008	Product Benchmark Outperformance	12.88% 6.68% 6.02%	13.52% 6.05% 7.47%	11.47% 5.84% 5.63%	12.25% 6.21% 6.04%		12.06% 7.05% 5.01%
Power Debt	STeFI Composite Index	Targets high cash returns through active interest rate risk management and yield enhancement. The Composite's weighted average rated credit quality must be a minimum of BBB. Investments in this product are limited to listed and unlisted assets in the power sector and supporting industries.	Paul Semple	May 2014	Product Benchmark Outperformance	10.91% 6.68% 4.23%					11.29% 6.43% 4.86%
INCOME											
Core Income	50% STeFI Call Deposit Index; 50% 3-7 Years All Bond Index	Aims to deliver excess return by investing in money market and bond assets with a focus on yield enhancement while limiting interest rate risk to a maximum average duration of two years.	Wikus Furstenberg	November 2002	Product Benchmark Outperformance	5.79% 5.89% -0.10%	5.61% 5.32% 0.29%	6.56% 6.03% 0.53%	7.00% 6.31% 0.69%	7.91% 7.20% 0.71%	8.53% 7.89% 0.64%
Flexible Income	110% SteFI Call Index	Aims to deliver excess return by investing in money market, bonds, preference shares and listed property and taking advantage of yield enhancement and capital growth opportunities. The composite is not limited by duration constraints.	Wikus Furstenberg	July 2006	Product Benchmark Outperformance	5.78% 6.56% -0.78%	5.81% 5.94% -0.13%	7.39% 5.81% 1.58%	7.82% 6.22% 1.60%		8.88% 7.20% 1.68%
Yield Enhanced Income	20% All Bond Index; 80% STeFI Composite Index	Aims to deliver excess returns through a combination of active interest rate risk management and yield enhancement by investing in listed and unlisted assets. Interest rate risk is constrained.	Wikus Furstenberg	May 2012	Product Benchmark Outperformance	7.38% 5.75% 1.63%	7.59% 5.55% 2.04%				8.23% 6.06% 2.17%

Product	Benchmark	Description	Portfolio manager	Inception date	Investment returns	1 Year	3 Years*	5 Years*	7 Years*	10 Years*	Since inception*
INTEREST RATE ASSET ALLOCATION											
Interest Rate Asset Allocation	ALBI (62.5%); JSE ILB IGOV Index (30%); STeFI Call Deposit Index (7.5%)	Aims to deliver excess return mainly through a combination of aggressive asset allocation within the various interest-bearing asset classes.	Wikus Furstenberg	July 2010	Product Benchmark Outperformance	2.23% 3.34% -1.11%	5.47% 4.16% 1.31%	9.60% 8.30% 1.30%			9.65% 8.62% 1.03%
INFLATION-LINKED BONDS											
Passive ILB Index	Barclays Capital/ Absa SAGILB	Aims to match the returns of the benchmark through passive interest rate and yield curve management.	Nazley Bardien	September 2005	Product Benchmark Outperformance	5.78% 5.94% -0.16%	5.48% 5.56% -0.08%	9.98% 10.14% -0.16%	9.38% 9.47% -0.09%	9.92% 10.03% -0.11%	10.16% 10.26% -0.10%
Core ILB	JSE ILB IGOV Index	Aims to deliver excess return through active interest rate risk management and limited yield enhancement.	Wikus Furstenberg	November 2005	Product Benchmark Outperformance	5.85% 5.70% 0.15%	5.39% 5.48% -0.09%	10.36% 10.09% 0.27%	10.01% 9.43% 0.58%		10.39% 10.11% 0.28%
Yield Enhanced Inflation-linked	RSA Inflation Linked Government Bond R202 Total Return Index	Targets high cash returns through a combination of active, real and nominal interest rate risk management and yield enhancement by investing in listed and unlisted assets.	Mei-Chi Liou	June 2011	Product Benchmark Outperformance	6.60% 4.99% 1.61%	9.03% 6.26% 2.77%				12.49% 10.49% 2.00%
Power Inflation-Linked***	RSA Inflation Linked Government Bond I2038 Total Return Index	Targets high cash returns through a combination of active, real and nominal interest rate risk management and yield enhancement by investing in listed and unlisted assets in the power sector and supporting industries.	Mei-Chi Liou	January 2014	Product Benchmark Outperformance	8.00% 4.94% 3.06%	10.10% 7.43% 2.67%				10.55% 8.27% 2.28%
Infrastructure & Development Inflation-linked	Barclays BESA SAGILB 15+	Targets high cash returns through a combination of active, real and nominal interest rate risk management and yield enhancement by investing in listed and unlisted socially responsible and developmental assets.	Mei-Chi Liou	Pending	Product Benchmark Outperformance	N/A					
NOMINAL BONDS											
Passive All Bond	All Bond Index	Aims to match the returns of the benchmark through passive interest rate and yield curve management.	Nazley Bardien	June 2000	Product Benchmark Outperformance	1.72% 1.75% 0.03%	3.24% 3.24% 0.00%	7.70% 7.71% -0.01%	8.17% 8.18% -0.01%	7.60% 7.60% 0.00%	10.84% 10.81% 0.03%
Core Bond	All Bond Index	Aims to deliver excess return through a combination of interest-bearing asset allocation, active duration management and yield enhancement.	Daphne Botha/ Wikus Furstenberg	January 2000	Product Benchmark Outperformance	1.67% 1.75% -0.08%	3.94% 3.24% 0.70%	8.37% 7.71% 0.66%	8.99% 8.18% 0.81%	8.29% 7.60% 0.69%	11.28% 10.69% 0.59%

Product	Benchmark	Description	Portfolio manager	Inception date	Investment returns	1 Year	3 Years*	5 Years*	7 Years*	10 Years*	Since inception*
NOMINAL BONDS cont.											
Long Duration Bond	All Bond Index 12+ Years	Aims to deliver excess return through active allocation between long-dated fixed rate and inflation-linked bonds, limited yield curve selection, duration management and yield enhancement.	Wikus Furstenberg	December 2006	Product Benchmark Outperformance	-1.59% -0.43% -1.16%	2.26% 2.22% 0.04%	7.65% 7.81% -0.16%	8.19% 8.05% 0.14%		7.47% 7.13% 0.34%
Yield Enhanced Bond	All Bond Index	Targets high cash returns through a combination of active interest rate risk management and yield enhancement by investing in listed and unlisted assets.	Jason Lightfoot	December 2001	Product Benchmark Outperformance	3.81% 1.75% 2.06%	6.32% 3.24% 3.08%	10.43% 7.71% 2.72%	10.98% 8.18% 2.80%	10.00% 7.60% 2.40%	11.13% 9.18% 1.95%
Infrastructure & Development Bond	All Bond Index	Targets high cash returns through a combination of active interest rate risk management and yield enhancement by investing in listed and unlisted socially responsible and developmental assets.	Jason Lightfoot	January 1995	Product Benchmark Outperformance	3.71% 1.75% 1.96%	6.16% 3.24% 2.92%	10.39% 7.71% 2.68%	11.18% 8.18% 3.00%	10.25% 7.60% 2.65%	12.67% 10.69% 1.98%
SOCIALLY RESPONSIBLE INVESTMENTS											
Infrastructure & Development Bond	All Bond Index	Targets high cash returns through a combination of active interest rate risk management and yield enhancement by investing in listed and unlisted socially responsible and developmental assets.	Jason Lightfoot	January 1995	Product Benchmark Outperformance	3.71% 1.75% 1.96%	6.16% 3.24% 2.92%	10.39% 7.71% 2.68%	11.18% 8.18% 3.00%	10.25% 7.60% 2.65%	12.67% 10.69% 1.98%
Development Equity	Consumer Price Index (CPI) + 10%	Targeting high returns by investing in equity and related assets that are socially responsible or develop-mental.	James Howard	September 2006	Product Benchmark	17.48% 16.29% 1.19%	17.17% 15.47% 1.70%	14.29% 15.66% -1.37%	14.45% 15.37% -0.92%		18.57% 16.33% 2.24%
Community Property	Consumer Price Index (CPI) + 4%	A portfolio specialising in the finance and development of retail shopping centres catering to the needs of under-serviced communi-ties throughout South Africa.	Smital Rambhai (Product Manager)	June 1996	Product Benchmark	17.95% 10.28% 7.67%	11.85% 9.46% 2.39%	10.60% 9.66% 0.94%	10.27% 9.36% 0.91%	12.75% 10.40% 2.35%	13.18% 9.91% 3.27%
Agri	Consumer Price Index (CPI) + 10%	A portfolio specialising in equity investments in agricultural land, agribusinesses and farming infrastructure.	Smital Rambhai (Product Manager)	March 2010	Product Benchmark	N/A					

Product	Benchmark	Description	Portfolio manager	Inception date	Investment returns	1 Year	3 Years*	5 Years*	7 Years*	10 Years*	Since inception*
SOCIALLY RESPONSIBLE INVESTMENTS cont.											
Development Balanced**	A composite weighting of the underlying funds' benchmarks.	A balanced portfolio providing investors with social impact from a targeted and development perspective and exposure to listed equities that track the JSE's SRI Index.	James Howard	November 2004	Product Benchmark Outperformance	0.43% -1.35% 1.78%	9.42% 7.94% 1.48%	10.16% 8.85% 1.31%	12.61% 11.66% 0.95%	10.60% 9.88% 0.72%	13.36% 12.55% 0.81%
Power Debt	STeFI Composite Index	Targets high cash returns through active interest rate risk management and yield enhancement. The Composite's weighted average rated credit quality must be a minimum of BBB. Investments in this product are limited to listed and unlisted assets in the power sector and supporting industries.	Paul Semple	May 2014	Product Benchmark Outperformance	10.91% 6.68% 4.23%					11.29% 6.43% 4.86%
Power Inflation-Linked***	RSA Inflation Linked Government Bond I2038 Total Return Index	Targets high cash returns through a combination of active, real and nominal interest rate risk management and yield enhancement by investing in listed and unlisted assets in the power sector and supporting industries.	Mei-Chi Liou	January 2014	Product Benchmark Outperformance	8.00% 4.94% 3.06%	10.10% 7.43% 2.67%				10.55% 8.27% 2.28%
Infrastructure & Development Inflation-Linked bond	Barclays BESA SAGILB 15+	Targets high cash returns through a combination of active, real and nominal interest rate risk management and yield enhancement by investing in listed and unlisted socially responsible and developmental assets.	Mei-Chi Liou	Pending	Product Benchmark Outperformance	N/A					

Currency: ZAR/Gross of fees

*Annualised
**Currently investors are Futuregrowth staff who may elect to invest through their retirement funds.
***Portfolio returns. Supplemental infomation.

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/ ASSET MANAGEMENT

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